

Office of the State Auditor

Division of State Audit

Comprehensive Annual Financial Report State of North Dakota

Audit Committee Communication and
Report on Internal Control, Compliance and
Other Matters
For the year ended June 30, 2007
Client Code 100

Robert R. Peterson
State Auditor



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Transmittal Letter

December 12, 2007

Legislative Audit and Fiscal Review Committee
Honorable John Hoeven, Governor
Members of the North Dakota Legislative Assembly
Pam Sharp, CPA, Director
Office of Management and Budget

I am pleased to submit our report on internal control, compliance, and other matters for the state of North Dakota. This report relates to the audit of the state's basic financial statements for the year ended June 30, 2007. This report on internal control, compliance, and other matters has been completed in accordance with *Government Auditing Standards*, as issued by the Comptroller General of the United States.

Also enclosed you will find our audit findings, audit committee communication, and related appendices. These communications are required by auditing standards.

The audit manager for this audit was Paul Welk, CPA. Inquiries or comments relating to this audit may be directed to Mr. Welk by calling him at (701) 328-2320. I would like to express my appreciation to Ms. Sharp and her staff for the courtesy, cooperation, and assistance they provided to this office during the audit.

Respectfully submitted,

Robert R. Peterson
State Auditor

Executive Summary

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

Responses to LAFRC Audit Questions

1. What type of opinion was issued on the financial statements?

An unqualified (clean) opinion was given on the state of North Dakota's financial statements.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

No. See the significant deficiencies included in this report under "Findings, Recommendations, and Management Response." Findings 07-1 through 07-4 are considered to be material weaknesses.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

No.

5. Has action been taken on findings and recommendations included in prior audit reports?

Yes, except Finding 07-1 is a prior recommendation that has not been implemented.

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

No.

LAFRC Audit Communications

1. Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.

There were no significant changes in accounting policies, and no management conflicts of interest or significant unusual transactions noted. The state's commitments and contingencies are reported on pages 107-110 of the Comprehensive Annual Financial Report.

2. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

Management's estimates of claim losses relating to insurance activities include Workforce Safety and Insurance, Risk Management Fund, and the Fire and Tornado Fund. For Workforce Safety and Insurance, actuaries are employed to assist in calculating the liability. Other auditors evaluated the key factors and assumptions used to develop the liability and the actuary's qualifications in determining that it is reasonable in relation to the financial statements taken as a whole. Estimated claim losses for the other insurance activities are made by professional insurance adjusters on a case by case basis. We evaluated the key factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Management's estimates of pension liabilities are based on valuation of actuarial amounts, provided by reputable actuaries. Other auditors evaluated the key factors and assumptions used to develop the liability and the actuaries' qualifications in determining that pension liabilities are reasonable in relation to the financial statements taken as a whole.

Management's estimate of the Medicaid liability is based on historical trends and analysis of individual components. We evaluated the key factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Allowance for loan losses and receivables are based on management's periodic review of their collectability in the light of historical experience, the nature of the receivable, adverse situations that may affect the borrower's ability to repay, and where applicable the value of any collateral and loan guarantees. Other auditors and we evaluated the key factors and assumptions used to develop the allowance in determining the allowances were reasonable in relation to the financial statements taken as a whole.

Tax refunds payable are based on historical trends and analysis of individual components. We evaluated the key factors and assumptions used to develop the liability in determining it is reasonable in relation to the financial statements taken as a whole.

3. *Identify any significant audit adjustments.*

Significant audit adjustments are included in Appendix A.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

We did not have any disagreements with management that were significant to the financial statements.

5. *Identify any serious difficulties encountered in performing the audit.*

We did not experience any serious difficulties in performing the audit.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

While OMB does employ consultants to assist in the preparation of the CAFR, we are not aware of any applicable management consultations with other accountants.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance and Human Resource Management System (HRMS) are the most high-risk information technology systems critical to the operations of the state. There are numerous other high-risk systems which are identified in the agency audit reports. The following significant deficiencies identified in the six audit report questions on page three of this report directly relate to these systems: Findings 07-1 and 07-2.

Report on Internal Control, Compliance, and Other Matters

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Honorable John Hoeven, Governor
of the State of North Dakota

Members of the Legislative Assembly
of the State of North Dakota

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the state of North Dakota as of and for the year ended June 30, 2007, which collectively comprise the state's basic financial statements and have issued our report thereon dated December 12, 2007. Our report was modified to include a reference to other auditors, for the emphasis of a matter (the actuaries for the ND Teachers' Fund for Retirement and the ND Public Employee Retirement System found the statutory contribution rates are insufficient) and as described in Note 18 to the basic financial statements, the Bank of North Dakota elected to present an unclassified balance sheet because the presentation of a classified balance sheet would be misleading to the extent that the financial statements may be materially misstated. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. As described in our report on the state of North Dakota's financial statements, other auditors audited the financial statements of the following entities:

Bank of North Dakota
Beginning Farmer Revolving Loan Fund
Board of University and School Lands
Building Authority
College SAVE Plan
Community Water Facility Loan Fund
Developmentally Disabled Facility
Loan Program
Guaranteed Student Loan Program
Housing Finance Agency

Job Service North Dakota
Mandan Remediation Trust
PACE and Ag PACE Funds
Public Employees Retirement System
Retirement and Investment Office
State Fair Association
Student Loan Trust
Workforce Safety and Insurance
All Discretely Presented Component Units

This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the North Dakota University System's component units were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the state of North Dakota's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the state of North Dakota's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the state of North Dakota's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of findings, recommendations, and management responses to be significant deficiencies in internal control over financial reporting.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 07-1 through 07-4 to be a material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the state of North Dakota's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The state of North Dakota's responses to the findings identified in our audit are described in the accompanying schedule of findings, recommendations, and management responses. We did not audit the state of North Dakota's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Office of Management and Budget and others within the state, Legislative Audit and Fiscal Review Committee, members of the North Dakota Legislative Assembly, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Robert R. Peterson
State Auditor

Paul A. Welk, CPA
Audit Manager

December 12, 2007

Findings, Recommendations, and Management Responses

Lack of General Ledger Transaction Approval Procedures (Prior Recommendation Not Implemented)

Finding 07-1

ConnectND does not have an online approval process for general ledger (GL) transactions. In addition, the Office of Management and Budget has not implemented controls to ensure state agencies have manual approval procedures. Without proper approval, internal control is compromised. This increases the risk of errors and fraud to unacceptable levels. These GL transactions can affect both revenues and expenditures of the state's various funds.

Recommendation:

We recommend the Office of Management and Budget implement ConnectND online approval for General Ledger transactions or provide guidance and training to agencies for alternative approval procedures.

OMB Response:

OMB agrees with the recommendation. ConnectND online approval for General Ledger transactions has been implemented.

Limiting Access to Information Technology Applications

Finding 07-2

Individuals have access to information technology applications beyond what is necessary to perform their job duties. We noted this security weakness at the following agencies with the applications shown in parenthesis:

- Office of Management and Budget - (ConnectND Human Resource Management System access granted by OMB to Information Technology Department employees).
- Department of Human Services - (Child Care Assistance, Vocational Rehabilitation Information System, Technical Eligibility Computer System, Comprehensive Child Welfare Information and Payment System, Low-Income Home Energy Assistance, Regional Office Automation Program, and VISION).
- Department of Public Instruction - (Foundation Aid and Food and Nutrition).

Policies and procedures should be in place to ensure: individuals only have access necessary to perform their job duties; an individual is assigned the responsibility of controlling access to all applications; and ongoing reviews are performed to ensure access rights are properly maintained. Without these controls, there is an increased likelihood of unauthorized access to confidential or sensitive information and fraud.

Recommendations:

We recommend agencies:

1. Establish policies and procedures to restrict access privileges to only necessary individuals.
2. Assign ongoing responsibility for security for each information technology application.
3. Perform continuing reviews of access privileges.

Agency Responses:

OMB agrees with the recommendation. We will periodically review and evaluate the security roles given to ITD developers to determine if they are necessary to perform their job duties.

The Department of Human Services will continue to enhance procedures surrounding access to technology applications.

The Department of Public Instruction concurs with the finding and has implemented procedures to comply with the recommendations.

Errors in Closing Packages and Adjusting Entries

Finding 07-3

Closing packages prepared by state agencies and used in the preparation of the state's Comprehensive Annual Financial Report contained several errors. We also noted several of the Office of Management and Budget's (OMB) adjusting entries were either made incorrectly or were not properly supported.

Several of the closing packages we tested contained errors, with the largest being \$12 million. Of the errors in OMB prepared adjusting entries, the largest two were reclassification errors of \$14.8 million and \$15.4 million. We noted other OMB prepared entries where the amounts were not properly supported. Had these errors not been detected during the CAFR audit, the state's financial statements would have been materially misstated.

Recommendation:

The Office of Management and Budget should address the problem of numerous errors occurring at the state agency and the CAFR compilation levels including:

- Evaluate the training needs for OMB and agency personnel including individuals that approve closing packages.
- Address control environment issues including: management's commitment to competency by ensuring closing packages are completed accurately; and management's philosophy and operating style by improving attitudes and actions toward financial reporting.
- Clearly communicate to the approvers of closing packages their duties and responsibilities.
- Monitoring and approval activities at OMB should be enhanced relating to both the review of agency closing packages as well as entries prepared by OMB staff and consultants.

Office of Management and Budget Response:

OMB partially agrees with this recommendation.

OMB provides agencies with closing package instructional manuals and provides assistance to agencies at their request. We conduct training sessions when there are significant changes to warrant these sessions. We plan to conduct training before the next CAFR.

We will again emphasize to agencies the importance of the closing packages to the CAFR, the need for all closing packages to be completed accurately, and will also remind approvers of closing packages of their responsibilities. However, we cannot ensure that addressing management's philosophy will improve attitudes toward financial reporting.

We plan to require state agencies to submit their CAFR information earlier in order to give us more time to review their closing packages and to prepare and review adjustments.

Lack of Proper Cash Reconciliation and Cash Balance Reporting at the Department of Transportation

Finding 07-4

The Department of Transportation (DOT) is not properly reconciling their motor vehicle clearing account to the report of amounts processed and pending each month. Due to a coding error in the Single State Registration System, DOT improperly transferred \$2.3 million from their motor vehicle clearing account to the Highway Fund from 2000-2007. DOT noticed the error and correctly transferred the money back to their clearing account in June 2007. Had the clearing account been properly reconciled, this coding error would have been detected promptly.

We also noted that DOT did not properly complete their Cash and Investments Summary Form closing package. This form is required by the Office of Management and Budget in preparing the state's Comprehensive Annual Financial Report (CAFR). On that form, DOT reported their entire unrecorded Bank of North Dakota cash balance in the Highway Fund. However, a material portion of the \$14 million unrecorded cash reported as belonging to the Highway Fund should have been allocated to other funds. Had the errors not been detected, it would have resulted in the state's financial statements being materially misstated.

Recommendations:

We recommend the Department of Transportation:

- 1) Properly reconcile their motor vehicle clearing account to the report of amounts processed and pending each month.
- 2) Properly complete their Cash and Investments Summary Form.

Department of Transportation Response:

NDDOT concurs with the findings and will implement the recommendations.

Establishing Adequate Fraud Programs and Controls

Finding 07-5

The state of North Dakota does not have adequate fraud programs and controls. This includes not having: 1) policies or procedures relating to a formal systematic risk assessment process which should include a thorough fraud risk assessment; 2) policies requiring agencies to have a comprehensive code of conduct; and 3) adequate policies relating to background investigations.

The most important guidance relating to internal control is contained in *Internal Control – Integrated Framework* published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This framework includes discussions about the importance of adequate risk assessment, code of conduct, and background investigations.

We are not aware of any state agency that has an adequate risk assessment process. Some state agencies have adequate codes of conduct, but many do not. OMB policy 112 “Employee Criminal History Background Checks” requires background checks for certain people who have access to personal information stored on the state’s PeopleSoft system. However, the policy does not include all individuals with access to personal information, positions of accounting and financial oversight, and positions of trust.

Without adequate fraud risk programs and controls the state exposes itself to risk of loss of assets, potential liabilities, and damage to the state’s reputation.

Recommendation:

We recommend the Office of Management and Budget ensure state agencies have adequate policies and procedures relating to: 1) formal systematic risk assessment process which includes a thorough fraud risk assessment; 2) comprehensive code of conduct; and 3) adequate background investigations.

Office of Management and Budget Response:

OMB agrees with the recommendation. We will review our statewide policies and develop additional policies or enhance current policies as needed.

Improper Financial Reporting by Information Technology Department

Finding 07-6

The Information Technology Department (ITD) did not include certain required financial information in their financial statements submitted for inclusion in the state’s Comprehensive Annual Financial Report (CAFR). However, once the omissions were brought to their attention, they revised their financial statements so that the correct amounts were included in the state’s CAFR.

Initially, ITD did not capitalize or report software purchases of \$5,000 or more from outside vendors as required by Office of Management and Budget fixed assets accounting policies. This resulted in an understatement of approximately \$2.8 million to net

capital assets. ITD also failed to report prepaid items as required by generally accepted accounting principles. These prepaid items were the portion of maintenance agreements which were paid in advance and extend beyond the current fiscal year. This resulted in an understatement to prepaid assets of approximately \$1.6 million.

Recommendation:

We recommend Information Technology Department include all required information in their financial statements submitted for inclusion in the state's Comprehensive Annual Financial Report.

Information Technology Department Response:

We agree with the recommendation and have already made changes to our accounting procedures to correctly account for capitalized software and prepaid items.

Improper Transaction Coding by Protection and Advocacy Project

Finding 07-7

The Protection and Advocacy Project incorrectly coded a transaction on the state's accounting system. Had this error not been detected by the Office of the State Auditor, it would have resulted in federal fund revenue and expenditures being understated by \$1 million in the state's Comprehensive Annual Financial Report.

The Protection and Advocacy Project received a \$1 million grant which they properly coded as revenue. However, when the grant funds were distributed they improperly coded them as a reduction of revenue instead of grant expenditures. Generally accepted accounting principles require transactions to be reported at their gross amount rather than their net amount.

Recommendation:

We recommend Protection and Advocacy Project properly record grant expenditures on the state's accounting system.

Protection and Advocacy Project Response:

The Protection and Advocacy Project agrees with the finding and will properly code such transactions in the future.

Audit Committee Communication

Legislative Audit and Fiscal Review Committee
North Dakota Legislative Assembly

We have audited the financial statements of the state of North Dakota for the year ended June 30, 2007, and have issued our report thereon dated December 12, 2007. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

As stated in our engagement letter dated July 20, 2007, and our report entitled "The Audit Process for the state of North Dakota" dated August 14, 2007, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

The management discussion and analysis is not a required part of the financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and expressed no opinion on it.

The combining and individual fund financial statements and schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information has been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and in our opinions, based on our audit and the reports of other auditors, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

As part of our audit, we considered the internal control of the state of North Dakota. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the state of North Dakota's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit.

Significant Accounting Policies

The Office of Management and Budget (OMB) has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by the state of North Dakota are described in Note 1 to the financial statements.

No new accounting policies were adopted that had a significant impact on financial reporting and the application of other existing policies was not changed during 2007.

We noted no transactions entered into by the state of North Dakota during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements are discussed below.

Management's estimates of claim losses relating to insurance activities include Workforce Safety and Insurance, Risk Management Fund, and the Fire and Tornado Fund. For Workforce Safety and Insurance, actuaries are employed to assist in calculating the liability. Other auditors evaluated the key factors and assumptions used to develop the liability and the actuaries' qualifications in determining that it is reasonable in relation to the financial statements taken as a whole. Estimated claim losses for the other insurance activities are made by professional insurance adjusters on a case by case basis. We evaluated the key factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Management's estimates of pension liabilities are based on valuation of actuarial amounts, provided by reputable actuaries. Other auditors evaluated the key factors and assumptions used to develop the liability and the actuaries' qualifications in determining that pension liabilities are reasonable in relation to the financial statements taken as a whole.

Management's estimate of the Medicaid liability is based on historical trends and analysis of individual components. We evaluated the key factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Allowance for loan losses and receivables are based on management's periodic review of their collectability in the light of historical experience, the nature of the receivable, adverse situations that may affect the borrower's ability to repay, and where applicable the value of any collateral and loan guarantees. Other auditors and we evaluated the key factors and assumptions used to develop the allowance in determining the allowances were reasonable in relation to the financial statements taken as a whole.

Tax refunds payable are based on historical trends and analysis of individual components. We evaluated the key factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For the purpose of this report, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our audit procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the state of North Dakota's financial reporting process (that is, cause future financial statements to be materially misstated). For the 2007 state CAFR audit, Appendix A contains the audit adjustments that, in our judgment, indicate matters that could have a significant effect on the state's financial reporting process.

In addition, Appendix B contains our "passed audit adjustments" which summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in aggregate, to the financial statements taken as a whole and to each reporting unit.

Disagreements with Management

For purposes of this report, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultation With Other Auditors

In some cases, management may decide to consult with other accountants about audit and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed with Management Prior to Retention

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention. It should be noted that the retention of the State Auditor is a matter of state law and is not under the control of the OMB.

Difficulties Encountered in Performing the Audit

We experienced no major difficulties relating to the performance of our audit or in dealing with management. We received full cooperation from management. We believe we have direct and unrestricted access to OMB employees and to management.

This information is intended solely for the information of the Legislative Audit and Fiscal Review Committee and management of OMB and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

We will be happy to discuss these or any other topics at your convenience. We would like to express our appreciation to the management of OMB for the cooperation we received during the course of our audit.

Paul Welk, CPA
Audit Manager

December 12, 2007

Appendix A – Audit Adjustments

Office of Management and Budget

Opinion Unit: Governmental Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Charges for Services	\$14,792,276	
Miscellaneous		\$14,792,276

Explanation: Office of Management and Budget failed to reclassify revenue that improperly rolled-up to Charges for Services revenue to Miscellaneous revenue.

Opinion Unit: Government Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Net Assets	\$15,360,900	
Net Assets, Invested in Capital Assets		\$15,360,900

Explanation: Office of Management and Budget debited Net Assets, Invested in Capital Assets in error.

Department of Transportation

Opinion Unit: Governmental Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Charges for Services	\$7,719,542	
Taxes		\$7,719,542

Opinion Unit: General Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Cash	\$7,017,765	
Revenue		\$7,017,765

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Revenue	\$7,701,765	
Cash		\$7,017,765

Explanation: To adjust for amounts reported on the cash and investment closing package that were incorrectly applied to fund 200.

Opinion Unit: Governmental Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Taxes	\$4,638,213	
Charges for Services		\$4,638,213

Opinion Unit: General Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Revenue	\$4,264,164	
Fund Balance – Prior Year		\$4,264,164

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Fund Balance – Prior Year	\$4,264,164	
Revenue		\$4,264,164

Explanation: This is a prior period adjustment to adjust for amounts reported on the 2006 cash and investment closing packages that were incorrectly applied to fund 200.

Opinion Unit: General Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Revenue	\$1,180,756	
Fund Balance – Prior Year		\$1,180,756

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Fund Balance – Prior Year	\$1,180,756	
Revenue		\$1,180,756

Explanation: This is a prior period adjustment to adjust for revenue from November 2000 through June 2006 that was not properly booked during that time.

Department of Human Services

Opinion Unit: Governmental Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Account Receivable	\$5,138,083	
Intergovernmental Receivable		\$5,138,083

Opinion Unit: Federal Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Account Receivable	\$5,138,083	
Intergovernmental Receivable		\$5,138,083

Explanation: When DHS prepared their Grant Receivable Closing Package they incorrectly included \$5,138,083 as amount received in July and applied back to June for draw-downs.

Information Technology Department

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Buildings and Equipment - Net	\$2,776,877	
Depreciation Expense	608,575	
Miscellaneous Revenue		\$1,558,343
Fund Balance – Prior Year		1,827,109

Explanation: Information Technology Department did not properly capitalize software purchased from outside vendors.

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Prepaid Items	\$1,580,044	
Operating Expenses		\$1,580,044

Explanation: Information Technology Department did not book the maintenance contracts that extend beyond June 30, 2007.

Tax Department

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Taxes Receivable - Net	\$5,579,605	
Deferred Revenue		\$5,579,605

Explanation: The Tax Department incorrectly reported a portion of Financial Institutions Tax as Uncollectable. All Financial Institutions Taxes are collectable.

Insurance Department

Opinion Unit: General Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Due from Other Funds	\$3,455,194	
Transfers In		\$3,455,194

Opinion Unit: Remaining Funds

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Transfers Out	\$3,455,194	
Due to Other Funds		\$3,455,194

Explanation: Adjustment to record this transfer in fiscal year 2007. Insurance Department had incorrectly reported it in fiscal year 2008.

Department of Health

Opinion Unit: Federal Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Revenue	\$2,392,804	
Inventory	213,829	
Expenditures		\$2,606,633

Explanation: General Fund Inventory, Revenue, and Expenditures were improperly booked to the Federal Fund. They had also been booked to the General Fund so there is no corresponding entry to the General Fund.

Protection and Advocacy

Opinion Unit: Governmental Activities

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Expenditures	\$1,000,000	
Revenue		\$1,000,000

Opinion Unit: Federal Fund

<u>Description</u>	<u>Debit</u>	<u>Credit</u>
Expenditures	\$1,000,000	
Revenue		\$1,000,000

Explanation: Protection and Advocacy improperly recorded a pass-through grant payment as a refund of revenue, rather than an expenditure.

Appendix B – Passed (Uncorrected) Audit Adjustments

Note: Errors below the Auditor's preliminary immateriality amounts are not included below.

1. Passed Audit Adjustment

Department of Corrections and Rehabilitation did not report expenditures on their closing package that were incurred in FY07 and paid for in FY08.

Entity-wide Statements	Debit	Credit
Governmental Activities		
Expenditures	\$606,460	
Accounts Payable		\$606,460
Fund Statement Effect		
General Fund		
Expenditures	148,092	
Accounts Payable		148,092
Remaining Funds		
Expenditures	458,368	
Accounts Payable		458,368

2. Passed Audit Adjustment

Office of Management and Budget did not reclassify the correct amount of operating grants to capital grants.

Entity-wide Statement Effect	Debit	Credit
Governmental Activities		
Operating Grants – Natural Resources	\$108,821	
Operating Grants - Transportation	680,000	
Capital Grants – Natural Resources		\$788,821

3. Passed Audit Adjustment

Office of Management and Budget booked a receivable to the State Historical Society Revolving fund that should have been booked to the federal fund.

Fund Statement Effect	Debit	Credit
Federal Fund		
Due from Other Funds	\$541,082	
Transfers In		\$541,082
Remaining Funds		
Transfers In	541,082	
Due from Other Funds		541,082

4. Passed Audit Adjustment

Office of Management and Budget made several errors when booking the government-wide adjustment for other long term debt.

Entity-wide Statement Effect	Debit	Credit
Governmental Activities		
Net Assets - Restricted	\$ 36,937	
Interest Payments	72,624	
Expenses – General Government	671,981	
Interest on Long-Term Debt		\$664,624
Accrued Interest Expense		36,937
Note Proceeds		43,044
Net Income Change		36,937